



EUROPEAN COMMISSION
DIRECTORATE-GENERAL FOR ENERGY

Directorate A - Energy policy
A.1 - Energy policy coordination

Brussels,
ENER A1/MCD

NOTE FOR THE FILE

Subject: Highlights and summary of the fourth meeting of the EU Refining Forum held on the 11th of December 2014

Overview

The fourth meeting of the EU Refining Forum took place on the 11th of December 2014.

More than 100 participants representing authorities and industry from a number of EU Member States, from the European Parliament and from various departments of the Commission attended the meeting.

The meeting was chaired by Mechthild Wörsdörfer, Director for Energy Policy, DG ENER.

The central focus of the meeting was the refining fitness check, the first preliminary results of which were delivered by the Commission.

Chris Beddoes, Director General of FuelsEurope and Concawe, provided an update on the situation of the EU refining industry since the last meeting of the Forum in May.

Sammy Six from the Clingendael Institute of International Relations reported on recent developments in global refining and in the supply and trade of petroleum products.

Francisco Caballero Sanz and Robert Marschinski, from the Commission, delivered the preliminary results of the refining fitness check.

A joint statement and requests to the Commission regarding the fitness check was issued from representatives of France, Germany, Italy, Ireland, Poland and the UK.

Béla Kelemen and Ilkka Räsänen, both executives from the industry (from, respectively, MOL Group and Neste Oil) and Members of the Board of FuelsEurope spoke about opportunities and threats in the EU refining sector.

Mr Kyrtos, MEP (EPP Group, member of ECON and BUDG Committees), provided the audience his perspectives as a Member of the new European Parliament on the EU refining sector's challenges and on the refining fitness check.

Gilberto Dialuce, Director General in the Italian Ministry of Economic Development, reported back on the Italian Presidency.

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Highlights & summary

Global refining margins are experiencing an upward trend as crude price declines have been more significant than petroleum product price falls.

Particularly strong gains in European refining margins, both in North Western Europe and the Mediterranean, have been observed in the last few months.

Refining margins have also been driven by US refinery outages which have contributed to falling demand for crude, and cheaper high quality oil from West Africa.

European oil demand for petroleum products continues to fall, especially strongly, compared to 2013, in Italy (-7.1%), France (-3.6%) and Germany (-3.5%).

(EU) Refiners are increasingly competing in a global rather than a regional market. How developments in other parts of the EU are intensifying competition for EU refiners:

- In the US, competitive refining operations based on the use of low cost crude oil and natural gas in highly efficient refineries have contributed to increasing refinery runs to support supply to export markets. As a result, US Gulf Coast refineries are exporting record amounts of products: ultra low sulphur diesel oil to Europe, gasoline to Mexico as well as to other parts of Latin America and West Africa. This is making it harder for surplus production of gasoline in Europe to find new markets.
- Middle Eastern refineries continue to be competitive relative to European refineries mainly due to economies of scale, state of the art projects, easy access to cheap crude and cheap labour.
- Russian simple refineries are undergoing gradual modernisation which will change the yield of Russia's barrel towards higher value products such as ultra low sulphur diesel oil destined for Europe.
- Apart from some Indian refineries that are already competing on the product (diesel) export market, also Chinese refineries are making increasing amounts of product available for export. International sales of diesel from Chinese refineries have for now mostly gone to Vietnam and Singapore, although more of them could soon end up all over the globe, including Europe.

Refining industry representatives from Hungary and Finland provided illustrations of how the industry continues to invest and innovate as well as to ensure compliance with environmental regulations even under such difficult, highly competitive market conditions.

The Commission delivered preliminary results of the refining fitness check, pointing out that not all pieces of legislation had been included in those results and that internal (Commission services) and external (stakeholders) consultations had not yet been carried out for all parts of the fitness check.

Going through individual pieces of legislation in turn, the Commission presented its assessment of the impacts on the refining industry either (i) on refinery operations or (ii) through product specification, both in terms of operating costs and associated capital investments, or impacts on the industry in terms of (iii) reductions in demand.

A key finding was that the key EU regulation analysed so far affecting the sector incurred an average cost of 40 eurocents per barrel during the years 2000 to 2012.

But the Commission explained that cost pass-through had not yet been analysed, and as such that it might reduce this number.

The Commission also reported on an assessment of the international competitiveness of the EU refining industry, also part of the fitness check exercise.

Reporting on the period between 2000 and 2012, the Commission highlighted that average refining net margins (gross margins less operating costs) in the EU had remained consistently below that of other regions of the world since 2006. This had essentially been due to constantly increasing operating costs over the period, of which increasing energy costs had been the main cause, mainly a consequence of relatively higher increases in energy prices in the EU compared to the rest of the world.

It was also highlighted that while over the period 2000-2012 the top 50% of EU refineries average fared better (in terms of net refining margins) than the average of the international competitors, the bottom 50% of EU refineries fared increasingly worse than the average of competitors.

Industry remarked that while the cost of EU regulation calculated by the Commission over the period 2000-2012 was substantial, the bulk of the costs to industry will come in future years, using the Industrial Emissions Directive and the sulphur in marine fuels directive as illustrations of that.

In response to the question whether EU legislation might have contributed to increased refining energy costs, the Commission suggested that it is currently analysing a series of working hypothesis on how this could have happened: EU ETS induced increased costs of purchased electricity; increased energy consumption due to the Fuel Quality Directive; a switch to low-sulphur crude oil for refinery energy due to pollution legislation (IED/LCPD/IPPCD); demand impacts (RED, ETD, IED) reducing utilisation rates, which can negatively affect refineries' energy efficiency.

In response to a statement that EU anti-fracking legislation was driving up EU energy prices and should therefore be included in the fitness check, the Commission said that this was not in the scope of the quantitative part of the fitness check but that it could be addressed in the qualitative part.

It was suggested to the Commission that an analysis of the variation in the cost-impact of legislation across EU regions should be included in the fitness check, just as analysis showing regional variations in refining margins was undertaken, to which the Commission responded that this could indeed be done.

The question was asked whether it was taken into account that different legislative impacts might be a consequence of different Member State implementation. The Commission replied that mostly refinery-level data was used in the analysis, which should reflect the end result of legislation and local-level implementation, but that there is no systematic comparison of implementation, although if considered important in studies on legislative effectiveness/efficiency reported in the fitness check, it would then also be reported.

A joint statement was delivered by MSs (FR, DE, IT, PL and the UK), containing the following requests:

- It asks that the fitness check be aligned with Member State studies and the need to explain why the fitness check comes to different conclusions.
- It reiterates the request made at the last meeting of the Forum in May 2014 to set up a working group, the main activities of which should include integrating the outcomes of Member States' studies in the fitness check, assist in developing the second stage of the fitness check, examine security of supply aspects and the resilience of the sector.
- It asks that the fitness check form a solid reference point for understanding the EU sector's competitive position, the cumulative effects and overlaps of past policy/legislation together with an assessment of threats from measures underway and that it provide a reference for any subsequent impact assessment on specific new pieces of legislation.
- The need to assess differences in implementation of EU legislation across the EU was also highlighted.

In response, the European Commission said that a working group has already been set up, meetings of which all Member State representatives had been invited. The Commission also promised that the refining fitness check will explain why some of the results are different from studies carried out by Member States.

In complement to the requests of Member States, which it fully endorsed, the industry spoke of the necessity to be given sufficient time for the work on the fitness check to be done properly.

Further, industry explained that a continued presence in Europe is still attractive in spite of falling demand, by virtue of the size of the market but highlighted that it depended on legislation that is fit for purpose, not overly burdensome as well as predictable and stable.

Industry also highlighted that the EU will continue to need oil products beyond 2030 and that while crude oil prices and availability are set by global markets, crude oil is unique among primary energy sources in needing processing (refining) to make useable products. Security of supply for EU consumers is best achieved by maintaining the strong internal products market through a competitive refining and distribution system.

Mr Kyrtos, MEP, reflected on the importance of the contribution of refineries in the Greek industry sector. He highlighted that given that public debt could not be increased to finance the recovery, conditions to enable the private sector to invest were crucial. He reflected on falling investments in the EU in spite of the ECB low interest policy and suggested that this was due to a lack of investment opportunities resulting, among other things, from too much locally-focussed policies. He spoke of the necessity of a common EU energy policy and enabling conditions for industry to invest without policies that impose an undue burden on citizens.

The Italian Presidency reiterated and emphasised the importance of the demands by Member States included in the joint statement and also underlined the importance of refining related conclusions of the Security of Supply Strategy Communication of May 2014, highlighting the recommendations to discuss with industry and Member States how to diversify crude oil supplies to EU refineries to reduce dependence on Russia and ensure that transparency of data on flows, investments, and ownership is promoted. It expressed the wish that the Latvian Presidency would follow-up on such initiatives.

The Commission reiterated the strategic importance of the refining industry in the EU and the importance of striking a balance between the EU's strong climate and environmental ambitions and ensuring that the best possible business conditions remain for industries such as oil refineries to stay in the EU.

The Commission also took the opportunity to highlight several proposals which it has made in recent months which have acknowledged and factored in potential detrimental impacts on the industry and which have represented reasonable compromises (the revision of the carbon leakage list, the proposal to extend this approach beyond the current phase of the ETS, the proposals on the Fuel Quality Directive's article 7a and the refining BREF of the Industrial Emissions Directive, which the Member States have supported).

The Commission concluded the meeting by assuring of the importance and continuity of the EU Refining Forum to maintain the exchange of views between stakeholders and EU institutions. In addition, efforts will be made to involve the Latvian Presidency in the discussions on the high-level follow ups to the refining fitness check and the possibility of the presence of Commissioner Miguel Arias Cañete at one of the next meetings of the Forum in 2015 will be looked into. Lastly, participants were invited for their input ahead of the Commission's proposal on the Energy Union, which is to be delivered early in 2015, covering the five dimensions outlined by Vice President Maroš Ševčovič: 1. Supply security, based on solidarity and trust; 2. A competitive and completed internal energy market; 3. Moderation of energy demand; 4. Decarbonisation of the EU energy mix and 5. Research and Innovation.

Finally, Mrs Wördörfer thanked all participants for an active and constructive meeting and discussions.

Background on the EU Refining Forum

On the 15th of May 2012, Commissioner Oettinger organised an EU Refining Roundtable, at which representatives of all 21 EU Member States with an oil refining presence, Members of the European Parliament as well as representatives of the EU refining industry and of trade unions were convened to share views on the difficulties faced by the EU oil refining sector and to assess the need for coordinated action at the EU level to deal with the sector's difficulties.

In response to requests by industry and Member States at the Refining Roundtable, the Commission then organised an EU Refining Conference on the 26th of November 2012. This conference provided stakeholders the opportunity to give their views on the Commission proposals for a horizontal sectoral fitness check of oil refining announced in October 2012 in the communication on industrial policy, and on the setting up of an EU Refining Forum.

The aim of the EU Refining Forum is to provide an opportunity for the industry, Member States, Members of the European Parliament, the Commission and other stakeholders to come together and discuss planned and future regulatory proposals with potentially significant impacts on the EU oil refining industry and on the EU's security of supply of petroleum products.